No. SC84917

IN THE SUPREME COURT OF MISSOURI

FALL CREEK CONSTRUCTION COMPANY, INC.

Appellant,

v.

DIRECTOR OF REVENUE,
STATE OF MISSOURI

Respondent.

ON PETITION FOR JUDICIAL REVIEW OF THE
DECISION OF THE MISSOURI ADMINISTRATIVE
HEARING COMMISSION

BRIEF OF APPELLANT

KENNETH N. HALL, #52474

HUSCH & EPPENBERGER, LLC
1949 E. Sunshine St., Suite 2-300
Springfield, Missouri 65804
PHONE: (417) 862-6726
FAX: (417) 862-6948

ATTORNEYS FOR APPELLANT
FALL CREEK CONSTRUCTION
COMPANY, INC.

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JURISDICTIONAL STATEMENT

Appellant Fall Creek Construction Company, Inc. seeks a reversal of the decision of the Administrative Hearing Commission with respect to the use tax imposed on Appellant's ownership interest in a fractional aircraft ownership program. This action involves an issue of first impression in Missouri, specifically, the construction of RSMo. §§ 144.030, 144.605(5), 144.605(10), 144.605(13), 144.610 and 49 U.S.C. § 40116 in the context of an ownership interest in a fractional ownership aircraft program. Accordingly, this case necessarily involves the construction of the revenue laws of the State of Missouri and this Court has exclusive jurisdiction of this appeal under Article V, section 3 of the Missouri Constitution.

STATEMENT OF FACTS

Fall Creek Construction Company, Inc. (hereinafter referred to as "Fall Creek") is a real estate development company with its principal place of business in Branson, Missouri. Fall Creek develops real estate in Missouri, Mississippi, Arizona and Virginia. (Tr. 13). As part of its business, Fall Creek's employees must travel to and from the locations at which it develops real estate.

On October 30, 1998, Fall Creek acquired, through a "fractional aircraft ownership program," a one-sixteenth (6.25%) undivided interest in a King Air B200 aircraft, tail number 713TA ("713TA") and a one-eighth (12.5%) undivided interest in a Beech Jet 400A aircraft, tail number N798TA ("798TA") from Raytheon Travel Air Company, a Kansas corporation ("Raytheon"). Fall Creek paid Two Hundred Fifty-four Thousand Dollars ($254,000.00) for its ownership interest in the 713TA and Seven Hundred Seventy-two Thousand Five Hundred Dollars ($772,500.00) for its ownership interest in the 798TA. (See Exhibit A to the 713TA and 798TA Purchase Agreements at pages 8 and 45 of Joint Exhibit A).

Raytheon provides flying services under what is generally called a fractional aircraft ownership program (the "Program"). (Tr. 26). As part of the Program, a participant buys a percentage interest in a particular airplane which, along with the participant's execution of other Program agreements, contractually entitles the participant to fly a certain number of hours in one of one hundred ten (110) aircraft in the Program. (Tr. 27, 28).

A condition to a participant's purchase of a percentage interest in an airplane is that the participant enter into an Aircraft Purchase Agreement (the "Purchase Agreement"), a Joint Ownership Agreement (the "Joint Ownership Agreement"), a Management Agreement (the "Management Agreement") and a Master Interchange Agreement (the "Master Interchange Agreement") (the Purchase Agreement, Joint Ownership Agreement, Management Agreement and Master Interchange Agreement are sometimes collectively referred to hereinafter as the "Governing Documents"). The Governing Documents for each of the two transactions in question are identical and were introduced into evidence as Joint Exhibit A[1].

Raytheon, as manager of the Program, provides the flying service either in the airplane in which the participant has purchased a share or in another airplane in the Program. (Tr. 28). Raytheon is responsible for in excess of one hundred ten (110) airplanes in the Program. Therefore, most of the time a participant flies in an airplane which it does not "own." (Tr. 28).

If a participant requires air transportation, the participant contacts Raytheon to advise that the participant needs to go to a certain destination. Raytheon arranges for a Program airplane to pick up the participant, take the participant to the destination, and drop the participant off. Raytheon further arranges for catering and ground transportation

[1] Each of the Governing Documents for 713TA and 798TA are identical. Accordingly, any reference to a particular section of a Governing Document refers to the same section of the Governing Document with respect to both 713TA and 798TA.

at the request of the participant and fully manages the airplane with regards to maintenance of the airplane, the crew and scheduling of the airplane. (Tr. 28). The participant controls only where the airplane flies. Raytheon, or the pilot of a particular airplane, determines whether an airplane will fly to a location due to problematic weather or legality issues. (Tr. 80).

Raytheon considers the participant in "operational control" of the airplane for the time that the participant is in the air due to the fact that the participant has the right to tell Raytheon to go to a different destination than originally scheduled. (Tr. 29) Once the participant leaves the airplane, the participant is no longer in control and Raytheon controls where the airplane goes next. (Tr. 29).

There are two types of maintenance that occur on the airplanes in the Program. Unscheduled maintenance generally occurs wherever the airplane is broken. Scheduled maintenance is based upon a required maintenance schedule. Scheduled maintenance can occur at one of several locations. (Tr. 30, 31).

There are three major airplanes in the Program: the Hawker 800XP, the Beechjet, and the King Air. The Hawker 800XP's regularly scheduled maintenance occurs in Little Rock, Arkansas. The Beechjet's regularly scheduled maintenance primarily occurs in Atlanta, Georgia. The King Air's regularly scheduled maintenance occurs at various locations across the country.

Raytheon can only predict twenty-four (24) hours in advance where each of the airplanes in the Program will be located. Raytheon uses an "optimization program" which looks at all the flight demands of the Program participants and determines which

airplane should fly which trips. The optimization program is used to minimize the cost to Raytheon. The minimization of cost does not decrease or otherwise impact the participant's cost of utilizing the Program. (Tr. 32).

A participant generally will ask for the type of airplane in which it owns an interest but it has a contractual right to fly in any of the other types of airplanes in the Program. (Tr. 33). The cost to the participant of utilizing a different airplane will increase or decrease depending on whether the participant moves up or down in airplane size. For example, consider a participant that owns an interest in a King Air entitling the participant to fly one hundred (100) hours per year in a King Air. For every hour that the participant flies in a King Air, the participant is charged one hour against the one hundred (100) hours the participant purchased. If the participant requests and flies in a Beechjet (which is a larger airplane), the participant consumes its purchased hours at a quicker rate. (Tr. 34).

The aircraft in the Program are typically not hangared unless they need to be hangared due to weather. (Tr. 35). The airplanes typically spend the night at the final destination for the day. The airplanes do not have a home base and are considered nomadic or transient. (Tr. 35).

The Purchase Agreement spells out the terms of the purchase of the fractionalized interest in a particular airplane from Raytheon. (Tr. 36). It identifies the purchase price, identifies the aircraft in which the participant is purchasing an interest, and spells out the terms and conditions for Raytheon buying the interest back when the participant chooses to exit the Program. (Tr. 36).

Some of the pertinent provisions in the Purchase Agreement are as follows: the participant's interest is subject to the rights of Raytheon and the additional participants in the Program; no participant may place a lien on the aircraft; after sixty (60) months, the participant must sell the interest back to Raytheon; transfers to third parties are conditioned upon meeting strict requirements of Raytheon; Raytheon has a right of first refusal; and at Raytheon's sole discretion, it can substitute the aircraft interest owned by the participant with another similar aircraft interest. (Joint Exhibit A, Purchase Agreement).

The Management Agreement spells out the rights and responsibilities between a participant and Raytheon with respect to the management of an aircraft. (Tr. 37).

Some of the pertinent provisions in the Management Agreement are as follows: Raytheon is responsible to have the aircraft inspected, maintained, serviced, repaired, overhauled, and tested; Raytheon is responsible to maintain all required aircraft records and logs; Raytheon provides pilots, pilot training, pilot medical examinations, and pilot uniforms; Raytheon provides hangaring and tie-down space, catering, flight planning, weather services, and communications; Raytheon maintains insurance on the airplane; and Raytheon provides consulting regarding Federal Aviation Administration issues, warranty claims, and insurance matters. (Joint Exhibit A, Management Agreement).

The Joint Ownership Agreement is an agreement between Raytheon and all the participants that own an interest in a particular aircraft. (Tr. 37). Under the Joint Ownership Agreement, the "owners" of a particular aircraft place the aircraft into the Master Interchange Program and agree that they are all tenants in common with respect to

the aircraft. (Joint Exhibit A, Joint Ownership Agreement § 3.2). The "owners" waive any right to partition and agree that the only means by which they can divest themselves of the interest would be in accordance with the Governing Documents. (Joint Exhibit A, Joint Ownership Agreement § 3.2). The participant's right to place a lien on the interest in the Program or the airplane itself is significantly limited. (Joint Exhibit A, Joint Ownership Agreement § 4.2). Each participant is entitled to use the aircraft for a defined and specific period of time each year. (Joint Exhibit A, Joint Ownership Agreement § 5.1).

The Master Interchange Program is the device that allows other participants in the Program to fly in all of the airplanes in the Program. (Tr. 38). Under the Master Interchange Agreement, each participant agrees to participate in the Program by sharing its aircraft and pilots with all other participants in the Program. (Joint Exhibit A, Master Interchange Agreement § 3.1). If a participant's airplane is unavailable, it is able to use another aircraft in the Program. (Joint Exhibit A, Master Interchange Agreement § 3.3). There are no additional charges for the use of an interchange aircraft unless the airplane is a different make or model than that "owned" by the participant and is specifically requested by the participant. (Joint Exhibit A, Master Interchange Agreement § 3.3).

The Governing Documents provide that the airplanes are delivered in Wichita, Kansas because Raytheon's headquarters are in Wichita and the sales tax laws in Kansas provide that no sales tax is collected if the airplane is removed from the State of Kansas within ten (10) days after the purchase. (Tr. 39).

Raytheon requires each participant to execute an irrevocable power of attorney which allows Raytheon to file the appropriate registration application with the Federal Aviation Administration on each occasion that new participants purchase an interest in a particular airplane. As a general rule, the other "owners" of a particular aircraft would not know that an additional interest in that aircraft had been sold. (Tr. 40).

If a participant uses up all its hours with respect to its interest in an airplane, that participant is entitled to borrow ahead up to twenty-five percent (25%) of one year's flying from the next year's flying. (Tr. 70). Once the participant utilizes all of its hours during the life of the program, the participant is no longer entitled to flying privileges but must continue to pay to have the airplane managed until the participant exits the Program. (Tr. 71).

On the Bill of Sale and the Aircraft Registration Application, the participant in the program is specified as the owner of a specific interest in a particular airplane. The Federal Aviation Administration recognizes the participant as the legal owner of the partial interest in a particular airplane. (Tr. 78).

Raytheon did not pay any sales or use tax to the States of Kansas or Missouri on the aircraft in question. (Tr. 78).

The original assessment under Use Tax Assessment No. 200103605970020[2] was Forty-three Thousand Three Hundred Sixty-nine and 63/100 Dollars ($43,369.63). (Tr. 87; Respondent's Exhibit 1).

The Use Tax Assessment is only on the purchase price of the percentage interest of the aircraft acquired by Fall Creek and not on the total value of the airplane. (Tr. 87).

Fall Creek did not pay sales tax to the State of Missouri on its purchase of the interests in the Program. (Tr. 88).

Between October 30, 1998 and December 31, 1999 (the "Audit Period"), the 713TA was involved in a total of eight hundred forty (840) flights over a period of four hundred twenty-eight (428) days. Twenty-six (26) of the flights involved arrivals in or departures from the State of Missouri. The 713TA stayed overnight in the State of Missouri a total of thirteen (13) times. During the Audit Period, Fall Creek utilized the 713TA eight (8) times. (Joint Exhibit C).

During the Audit Period, the 798TA was involved in a total of eight hundred ninety-seven (897) flights over a period of four hundred twenty-four (424) days. Sixteen

[2] The Department originally made an additional assessment, No. 2001103605970021, in the amount of Seventeen Thousand Eighty-three and 79/100 Dollars ($17,083.79) with respect to the acquisition of an additional aircraft (referred to at the Administrative Hearing Commission hearing as the "600TA"). This assessment was withdrawn by the Department and the parties stipulated that the Administrative Hearing Commission would not consider any information concerning the acquisition of the 600TA.

(16) of the flights involved arrivals in or departures from the State of Missouri. The 798TA stayed overnight in the State of Missouri a total of eleven (11) times. During the Audit Period, Fall Creek utilized the 798TA three (3) times. (Joint Exhibit C).

During the Audit Period, Fall Creek utilized the Program by taking sixty-seven (67) flights which originated in Missouri and sixty-seven (67) flights which arrived in Missouri. The total number of intrastate flights during the Audit Period was fourteen (14). Fall Creek had no intrastate flights utilizing the 713TA or 798TA. (Joint Exhibit D).

On April 13, 2001, Fall Creek filed a Complaint with the Administrative Hearing Commission (the "AHC") challenging the final decision of the Director of Revenue (the "Director") assessing its use tax. (LF, 1-11). On January 15, 2002, the AHC convened a hearing on the Complaint, at which hearing testimony and documents were submitted as evidence. On October 18, 2002, the AHC issued its decision concluding that Fall Creek was responsible for payment of the full amount of the use tax assessed on Fall Creek's ownership interest in the Program. (LF, 23-29; Appendix at Page A-1).

POINTS RELIED ON

I. THE ADMINISTRATIVE HEARING COMMISSION ERRED IN CONCLUDING THAT FALL CREEK IS RESPONSIBLE FOR PAYMENT OF USE TAX ON ITS OWNERSHIP INTEREST IN A FRACTIONAL AIRCRAFT OWNERSHIP PROGRAM, BECAUSE THE INTERESTS IN EACH AIRCRAFT CONVEYED TO FALL CREEK DO NOT CONSTITUTE "TANGIBLE PERSONAL PROPERTY" UNDER § 144.610, RSMo. 2000, IN THAT THE SUBSTANCE OF THE TRANSACTION IN QUESTION WAS THAT FALL CREEK PURCHASED NOT TANGIBLE PROPERTY BUT ONLY THE RIGHT TO USE ANY ONE OF ONE HUNDRED TEN (110) AIRCRAFT FOR A SPECIFIED NUMBER OF HOURS PER YEAR AND THAT SUCH RIGHT TO USE THE AIRCRAFT IS A NONTAXABLE SERVICE.

Executive Jet Aviation, Inc. v. United States, 125 F.3d 1463 (Fed. Cir. 1997)

Gap, Inc., Adv. Op., Comm T and F, TSB-A-00(3)S(1-28-2000)

Sneary v. Director of Revenue, 865 S.W.2d 342 (Mo.banc 1993)

§ 144.030, RSMo. 2000

§ 144.610, RSMo. 2000

II. THE ADMINISTRATIVE HEARING COMMISSION ERRED IN CONCLUDING THAT FALL CREEK IS RESPONSIBLE FOR PAYMENT OF USE TAX ON ITS OWNERSHIP INTEREST IN A FRACTIONAL AIRCRAFT OWNERSHIP PROGRAM, BECAUSE THE IMPOSITION OF THE USE TAX ON SUCH PROGRAM IS AN IMPERMISSIBLE BURDEN ON INTERSTATE COMMERCE IN VIOLATION OF THE COMMERCE CLAUSE OF THE UNITED STATES CONSTITUTION AND § 144.030, RSMo. 2000, IN THAT THE NUMBER OF FLIGHTS TAKEN INTO MISSOURI BY 713TA AND 798TA FOR THE TAXPAYER'S BUSINESS DO NOT CREATE A SUBSTANTIAL NEXUS UNDER THE TESTS SET FORTH BY THIS COURT IN *DIRECTOR OF REVENUE V. SUPERIOR AIRCRAFT LEASING CO.*

Complete Auto Transit, Inc. v. Brady, 430 U.S. 274 (1977)

Director of Revenue v. Superior Aircraft Leasing Co., 734 S.W.2d 504 (Mo.banc 1987)

King v. L & L Marine Service, 647 S.W.2d 524 (Mo.banc 1983)

§ 144.030, RSMo. 2000

III. THE ADMINISTRATIVE HEARING COMMISSION ERRED IN CONCLUDING THAT FALL CREEK IS RESPONSIBLE FOR PAYMENT OF USE TAX ON ITS OWNERSHIP INTEREST IN A FRACTIONAL AIRCRAFT OWNERSHIP PROGRAM, BECAUSE FALL CREEK HAS NOT EXERCISED SUFFICIENT DOMINION OR CONTROL OVER THE INTERESTS IN EACH AIRCRAFT TO CONSTITUTE "STORAGE" OR "USE" OF AN AIRCRAFT IN THE STATE OF MISSOURI UNDER §§ 144.610 AND 144.605(13), RSMo. 2000, IN THAT RAYTHEON MAINTAINED CONTROL OF THE AIRCRAFT AND FALL CREEK MERELY CONTACTED RAYTHEON TO REQUEST TRANSPORTATION TO A PARTICULAR LOCATION.

§ 144.605(13), RSMo. 2000

§ 144.610, RSMo. 2000

IV. THE ADMINISTRATIVE HEARING COMMISSION ERRED IN CONCLUDING THAT FALL CREEK IS RESPONSIBLE FOR PAYMENT OF USE TAX ON ITS OWNERSHIP INTEREST IN A FRACTIONAL AIRCRAFT OWNERSHIP PROGRAM, BECAUSE THE INTEREST IN THE AIRCRAFT PURCHASED BY FALL CREEK DID NOT "FINALLY COME TO REST" WITHIN THE STATE OF MISSOURI AS REQUIRED BY § 144.610, RSMo. 2000, IN THAT THE UNDISPUTED EVIDENCE SUBMITTED AT THE HEARING BEFORE THE ADMINISTRATIVE HEARING COMMISSION INDICATES THAT 713TA AND 798TA NEVER CAME TO REST IN THE STATE OF MISSOURI.

Director of Revenue v. Superior Aircraft Leasing Co., 734 S.W.2d 504 (Mo.banc 1987)

Nubo, Ltd. v. Director of Revenue, No. RS-84-1778 (Mo. Administrative Hearing Commission, December 30, 1987)

§ 144.610, RSMo. 2000

LEGAL ARGUMENT

I. THE ADMINISTRATIVE HEARING COMMISSION ERRED IN CONCLUDING THAT FALL CREEK IS RESPONSIBLE FOR PAYMENT OF USE TAX ON ITS OWNERSHIP INTEREST IN A FRACTIONAL AIRCRAFT OWNERSHIP PROGRAM, BECAUSE THE INTERESTS IN EACH AIRCRAFT CONVEYED TO FALL CREEK DO NOT CONSTITUTE "TANGIBLE PERSONAL PROPERTY" UNDER § 144.610, RSMo. 2000, IN THAT THE SUBSTANCE OF THE TRANSACTION IN QUESTION WAS THAT FALL CREEK PURCHASED NOT TANGIBLE PROPERTY BUT ONLY THE RIGHT TO USE ANY ONE OF ONE HUNDRED TEN (110) AIRCRAFT FOR A SPECIFIED NUMBER OF HOURS PER YEAR AND THAT SUCH RIGHT TO USE THE AIRCRAFT IS A NONTAXABLE SERVICE.

A. Standard of Review.

On factual questions, the Supreme Court "considers whether a decision of the Administrative Hearing Commission is supported by substantial evidence upon the record as a whole. . . ." *Gammaitoni v. Director of Revenue*, 786 S.W.2d 126, 128 (Mo. banc 1990). In contrast, this Court's review of legal questions is *de novo*: "As to questions of law, this Court is not bound by the determinations of the Administrative Hearing Commission, but conducts a *de novo* review." *Delta Airlines, Inc. v. Director of*

Revenue, 908 S.W.2d 353, 355 (Mo. banc 1995). When the issue presented on appeal is the construction and application of the law to facts, the issue is one of law. *Division of Employment Security v. Taney County R-III*, 922 S.W.2d 391, 393 (Mo. banc 1996).

There is very little, if any, factual dispute in this case. With respect to the argument made in this section of the Brief, the issue is whether the AHC erred in ruling that the "interest" purchased by Fall Creek constitutes tangible personal property, as required by § 144.610, RSMo. 2000. Accordingly, this Court's review on this issue is *de novo*.

B. Legal Authority.

The Missouri Compensating Use Tax Law, §§ 144.600 to 144.761, RSMo. 2000 (the "Use Tax"), is designed to tax out-of-state purchases of tangible personal property by Missouri residents who use the property within the state. Section 144.610 sets forth the general requirements for the imposition of the use tax. That section, in part, provides:

> A tax is imposed for the privilege of storing, using or consuming within this state any article of tangible personal property purchased on or after the effective date of sections 144.600 to 144.745 in an amount equal to the percentage imposed on the sales price in the sales tax law in section 144.020.

By its terms, the Use Tax applies only to the storage, use, or consumption of *tangible personal property*.

The statutes do not provide a definition distinguishing tangible personal property from intangible personal property.

Black's Law Dictionary (7th ed. 1999) defines tangible personal property as: "corporeal personal property of any kind; personal property that can be seen, weighed, measured, felt, or touched, or is in any way perceptible to the senses."

The Missouri Supreme Court has consistently held that the "true object" or "essence of the transaction" determines whether a transaction should be treated as a taxable transfer of tangible personal property or as a nontaxable performance of a service. The analysis focuses on the substance of the transaction to determine the real object that the buyer seeks. *Sneary v. Director of Revenue*, 865 S.W.2d 342 (Mo.banc 1993); *K&A Litho Process, Inc. v. Director of Revenue*, 653 S.W.2d 195 (Mo.banc 1983); *James v. Tres Computer Sys., Inc.*, 642 S.W.2d 347 (Mo.banc 1982).

C. Legal Analysis.

The substance of the transaction between Raytheon and Fall Creek, evidenced by reading all provisions in the Governing Documents and reviewing the testimony submitted at the AHC hearing, was that Raytheon sold to Fall Creek the right to use any one of one hundred ten (110) aircraft for a specified number of hours per year to transport Fall Creek's employees to and from its places of business.

Pursuant to the Purchase Agreement and the Bill of Sale, Fall Creek purchased from Raytheon an "interest" in what appears to be a specific airplane. However, Raytheon's obligation to sell the interest to Fall Creek was expressly conditioned upon Fall Creek becoming a party to the other Governing Documents. Accordingly, it is critical to evaluate the effect those Governing Documents had on the purchase.

The Purchase Agreement generally spells out the terms of the purchase of a percentage interest in a particular airplane. This agreement identifies the purchase price, identifies the aircraft in which the participant is purchasing an interest, and spells out the terms and conditions for Raytheon's repurchase of the percentage interest when the participant chooses to exit the Program.

Importantly, the Purchase Agreement specifically provides that the interest acquired is subject to the respective obligations and rights of Fall Creek, Raytheon, and additional interest owners as provided in all Governing Documents. (Joint Exhibit A, Purchase Agreement § 2.1). Except for the limited circumstances set forth in the Joint Ownership Agreement, no participant is allowed to place a lien on the aircraft. (Joint Exhibit A, Purchase Agreement § 2.2.1). After twenty-four (24) months, Fall Creek has the absolute right to sell the interest back to Raytheon for the lesser of the purchase price or fair market value of the interest. (Joint Exhibit A, Purchase Agreement § 6.2.1). After sixty (60) months, Fall Creek is obligated to sell its interest in the airplane back to Raytheon. (Joint Exhibit A, Purchase Agreement § 6.2.2.1).

Fall Creek could only sell its interest to a third party on the condition that (a) Raytheon was the exclusive agent for the purpose of completing the transfer of the interest; (b) the Governing Documents were concurrently transferred to, and accepted by, the transferee; (c) the transferee was acceptable to Raytheon; (d) the transferee was a citizen of the United States or otherwise eligible to register an aircraft with the FAA; and (e) the transferee executed any documents necessary to reflect its participation in the Program. (Joint Exhibit A, Purchase Agreement § 7.1).

Under the Purchase Agreement, Raytheon was granted a right of first refusal in the event Fall Creek decided to sell its interest. (Joint Exhibit A, Purchase Agreement § 7.2). In the event of a total loss of the airplane, Raytheon was allowed to simply replace the airplane and the Program would continue. (Joint Exhibit A, Purchase Agreement § 7.4.1). At any time and at Raytheon's sole discretion, Raytheon could substitute an interest in another aircraft of the same make, model, and fair market value as Fall Creek's aircraft. (Joint Exhibit A, Purchase Agreement § 7.5).

Under the Joint Ownership Agreement, all "owners" of an interest in a particular airplane agreed to place the airplane into the Master Interchange Program. (Joint Exhibit A, Joint Ownership Agreement § 1.3). The "joint owners" agreed that they were tenants in common with respect to the aircraft. However, each of them waived any right they may have had to demand the partition, or sale for partition, of the aircraft. Each "joint owner" also agreed that the sole means by which it could divest itself would be in accordance with the Governing Documents. (Joint Exhibit A, Joint Ownership Agreement § 3.2). Under this agreement as well, no "joint owner" is authorized to put a lien on the "owner's" interest or the aircraft except (a) mechanic's liens to be discharged in the ordinary course of business and/or (b) a lien in favor of Raytheon Aircraft Credit Corporation. (Joint Exhibit A, Joint Ownership Agreement § 4.2). The lien in favor of Raytheon Aircraft Credit Corporation was required to be in a form acceptable to Raytheon. The lien was (a) limited to the interest of the borrowing "owner," (b) required to recognize the rights of other "joint owners" and Raytheon, and (c) required to contain a provision authorizing the aircraft to continue to be operated under the Management

Agreement and Master Interchange Agreement. (Joint Exhibit A, Joint Ownership Agreement § 4.2.1).

Each participant was entitled to use of the aircraft for a defined and specified period of time each year. No participant could operate the aircraft in excess of its allocated hours. (Joint Exhibit A, Joint Ownership Agreement § 5.1).

The Management Agreement generally provided that Fall Creek, along with the other "owners" of the particular aircraft, engaged the services of Raytheon to manage the aircraft for the benefit of the participants.

Raytheon was to arrange for the aircraft to be inspected, maintained, serviced, repaired, overhauled, and tested in accordance with approved maintenance programs including the standards and guidelines established by the Federal Aviation Administration and the aircraft manufacturer's recommended maintenance. Raytheon was obligated to keep the aircraft in good operating condition and in such condition necessary to maintain the airworthiness certification of the aircraft. (Joint Exhibit A, Management Agreement § 4.1). Raytheon was to maintain all aircraft records, logs, and Federal Aviation Administration materials on behalf of the participant. (Joint Exhibit A, Management Agreement § 4.2). Raytheon was to provide professionally trained and qualified pilots, recurrent pilot training, and pilot medical examinations and uniforms. (Joint Exhibit A, Management Agreement § 4.4). Raytheon was to provide (a) hangar, general storage and tie-down space, as necessary; (b) in-flight catering; (c) flight planning and weather services, communications, and a computerized maintenance program. (Joint Exhibit A, Management Agreement § 4.5). If requested by the

participant, Raytheon was to arrange for ground transportation at the expense of the participant. (Joint Exhibit A, Management Agreement § 4.6). Raytheon was to arrange and maintain insurance for the aircraft. (Joint Exhibit A, Management Agreement § 4.7.1).

Raytheon was to provide assistance to and consult with the participant on certain matters including (a) Federal Aviation Administration and manufacturer's correspondence and directives; (b) administration and enforcement of warranty claims; (c) administration and enforcement of insurance matters; (d) parts replacement and maintenance services; (e) preparation and filing of Federal Aviation Administration and federal communications commission mandatory reports and registrations; (f) services necessary to enable owner to participate in the Program; and (g) filing of documents as necessary and appropriate to perfect encumbrances created by the Governing Documents. (Joint Exhibit A, Management Agreement § 4.8).

Unless otherwise stated in the Governing Documents, the services provided were at Raytheon's sole cost and expense. (Joint Exhibit A, Management Agreement § 4.9). Participant was to pay Raytheon a monthly management fee. (Joint Exhibit A, Management Agreement § 5.1). Participant was to pay Raytheon a variable hourly rate. (Joint Exhibit A, Management Agreement § 5.2). The monthly management fee and variable hourly rate could, in Raytheon's sole discretion, be adjusted based upon a Consumer Price Index formula. (Joint Exhibit A, Management Agreement § 5.3.1). The variable hourly rate could be increased, in Raytheon's sole discretion, after a twenty-four (24) month period. (Joint Exhibit A, Management Agreement § 5.3.2).

Raytheon was authorized to use the aircraft for Raytheon's pilot's flight training and sales demonstration flights. (Joint Exhibit A, Management Agreement § 5.11).

The participant was entitled to use the aircraft up to a certain number of hours. (Joint Exhibit A, Management Agreement § 6.1). If a participant used all of its allotted hours during a particular year, the participant could borrow up to 25% of the next year's allotted hours. (Joint Exhibit A, Management Agreement § 6.1.2). Once these hours were used, the participant could not use any aircraft in the Program. (Tr. 71). Raytheon was to use reasonable efforts to obtain the participant's aircraft for the participant before providing an interchange aircraft. (Joint Exhibit A, Management Agreement § 6.2). If the participant's aircraft or an interchange aircraft was unavailable, Raytheon was to provide a suitable and comparable substitute aircraft. (Joint Exhibit A, Management Agreement § 6.3).

Under the Master Interchange Agreement, each participant agreed to participate in the Program and to share its aircraft and pilots with all other participants in the Program. (Joint Exhibit A, Master Interchange Agreement § 3.1). Each participant operating an interchange aircraft was considered to be in operational control of the interchange aircraft during its use. (Tr. 29, Joint Exhibit A, Master Interchange Agreement § 3.2). If a participant's airplane was unavailable, it could use an interchange aircraft. (Joint Exhibit A, Master Interchange Agreement § 3.3). There were no charges for use of an interchange aircraft unless it was of a different make or model and that interchange aircraft was specifically requested by the participant. Any additional charges were

charged against the participant's unused annual allocated hours referenced in the Management Agreement. (Joint Exhibit A, Master Interchange Agreement § 3.3.1).

The AHC's decision in this matter reveals that the AHC did not thoroughly review the Governing Documents and testimony to determine the substance of this transaction. Rather, the AHC decision focuses on the Bill of Sale and Purchase Agreement and wholly fails to acknowledge that the Bill of Sale and Purchase Agreement were conditioned upon numerous other contractual obligations.

In its argument to the AHC, Fall Creek submitted authority from other states and a federal court to suggest that these types of programs had previously been found to be transportation services, rather than tangible personal property. The AHC's analysis in this regard was cursory and does not address the points made by Fall Creek. Accordingly, it is necessary that Fall Creek again state its position with respect to that legal authority.

To date, the states that have addressed the application of a sales or use tax to a taxpayer's participation in a fractional aircraft ownership program are New York and Texas.

In *Gap, Inc.*, Adv. Op., Comm T and F, TSB-A-00(3)S(1-28-2000) (a copy of which is set out in the Appendix to this Brief at Page A-41), the Commissioner of the New York Department of Taxation and Finance ("NY Commission") issued an advisory opinion (the "Advisory Opinion") finding that a fractional program was a nontaxable transportation service.

The issue in the Advisory Opinion was whether taxpayer's purchase of a twenty-five percent (25%) interest in a noncommercial aircraft, where delivery was taken outside of New York State, was subject to the New York State Compensating Use Tax.

Taxpayer was a California corporation with merchants in New York State. Taxpayer purchased a twenty-five percent (25%) undivided interest in a noncommercial aircraft (the "Aircraft") to be used for transportation of its company personnel through the following arrangement.

Taxpayer entered into a Purchase Agreement by which it was obligated to become a party to a Management, Joint Ownership and Master Interchange Agreement. The Purchase Agreement, Management Agreement, Joint Ownership Agreement and Master Interchange Agreement described in the Advisory Opinion appear to be identical to the Governing Documents. The Advisory Opinion outlines the pertinent provisions of these agreements and it would be repetitive for Fall Creek to list them in this Brief. The ruling is not lengthy and the similarities between this case and the New York case are obvious upon a brief review of the Advisory Opinion.

The NY Commission held that the possession, command, and control of the Aircraft had not been transferred to the taxpayer and that what was being furnished to the taxpayer was a nontaxable transportation service and not a taxable purchase or rental of tangible personal property.

The AHC's interpretation of the Advisory Opinion is that the interchange program discussed in the Advisory Opinion was determined to be exempt from New York compensating use tax because the possession, command and control of the aircraft was

not transferred to the purchaser under New York law. The AHC determined that Missouri did not have a similar provision of law[3], and accordingly, found that the Advisory Opinion did not support Fall Creek's position. What the AHC failed to address is that the Advisory Opinion further states that what was being furnished to the taxpayer was a non-taxable transportation service and not a taxable purchase or rental of tangible personal property. This is exactly what Fall Creek is arguing. The AHC failed to address this argument.

In the December 2000 issue of "Tax Policy News," the Texas Comptroller issued a "FYI: Sales Tax," explaining the treatment of a fractional aircraft interchange program for Texas Sales and Use Tax purposes (a copy of which is set out in the Appendix to this Brief at page A-54). The article explained that there were four (4) major agreements involved in a fractional interest program. The Comptroller further stated that "the four (4) agreements must be construed together, in order to determine the parties intent." The Comptroller noted that the Internal Revenue Service had ruled that, for excise tax purposes, fractional ownership plans were more in the nature of a commercial transportation service than a co-tenancy because the owners had surrendered possession, command, and control of the aircraft. The Comptroller concluded that, although the participant in the program provided some direction, the possession of the aircraft

[3] Missouri does have a similar provision. RSMo. 2000, § 144.605(13) defines the term "use" as exercising a right over property incident to the control of that property. This issue is addressed in Point III of this Brief.

remained with the seller of the interest. The Comptroller concluded that the participant was contracting for a nontaxable air charter service and that a taxable sale or rental of an aircraft did not occur.

With respect to the Texas Comptroller's determination, the AHC simply states that such statement did not cite to any provision of law. Presumably, therefore, the AHC did not even consider the Texas Comptroller's position. To the contrary, the Texas Comptroller specifically references Internal Revenue Service rulings, to be discussed hereinafter.

In *Executive Jet Aviation, Inc. v. United States*, 125 F.3d 1463 (Fed. Cir. 1997), the Court of Appeals held that Executive Jet Aviation ("EJA") was engaged in a transportation business under a fractional aircraft ownership program.

The question in *Executive Jet* was whether EJA was subject to tax under I.R.C. § 4041 or I.R.C. § 4261. Generally, Section 4041(c) imposed a fuel tax on noncommercial flights. Noncommercial flights were defined as the use of an aircraft, other than use in the business of transporting persons or property for compensation or hire by air. If EJA was in the business of transporting persons or property for compensation, EJA's flights would be considered commercial flights and EJA would be subject to the transportation tax under § 4261.

EJA was an aircraft management and air charter service company. EJA ran a "NetJets" program.

A participant in the NetJets program was required to own or lease an interest in an aircraft. When entering the program through a purchase, the participant purchased a

percentage interest in an aircraft under a Purchase Agreement and Bill of Sale. As a condition precedent to the closing of the purchase, the participant was required to enter into a Management Agreement, an Owners Agreement (with the other parties holding interest in the aircraft), and a Master Interchange Agreement. Under the Purchase Agreement, the participant could not sell its interest in the aircraft without the prior written consent of Executive Jet Sales (the corporation from whom the aircraft were sold). The transfer was subject to the transferee assuming all of the participant's obligations under the various agreements.

Under the agreements, a participant in the NetJets program was entitled to a certain amount of flight time per year. However, the aircraft would be maintained, fueled, hangared, and insured by EJA, with pilots being selected by EJA.

Pursuant to the Management Agreement, EJA assumed full responsibility for maintenance and operation of the airplane. EJA inspected, serviced, repaired, overhauled, and tested the aircraft so that it was in compliance with FAA requirements. EJA maintained all records and logs as required by the FAA. EJA paid for fuel and the costs of the pilots and crew. EJA paid hangar and tie down costs, landing fees, food and beverage expenses and the expenses of flight planning. EJA selected the pilots. EJA obtained insurance with respect to the aircraft. A participant could substitute its own pilots, provided that they met EJA's requirements.

The participants in the NetJets program paid EJA a monthly management fee and an hourly rate charge. EJA was allowed to use the airplane when it was not otherwise in

use so that it could provide air transportation service to the public and flight training for its pilots.

The Interchange Agreement was executed by all of the owners in an aircraft and allowed the owners to participate in the interchange arrangement. The interchange arrangement allowed each owner or each participant to use another program aircraft if the participant was unable to use the aircraft in which it owned an interest. If the request was made for a different make and model airplane, the differential in the cost was charged against the owner's unused flight hours.

In *Executive Jet*, Texaco Air ("Texaco") acquired a 50% undivided interest in a particular airplane in order to become a participant in the NetJets program. Texaco executed all of the related agreements.

EJA paid the "non-commercial flights" Section 4041(c) tax. The IRS concluded that EJA was actually providing commercial transportation, taxable under I.R.C. § 4261. EJA paid a portion of the Section 4261 tax and filed a refund claim. The refund claim was disallowed and EJA filed a complaint in the Court of Federal Claims. The Court of Federal Claims concluded that EJA was involved in the business of providing transportation for compensation or hire. EJA appealed the case.

In its appeal, EJA asserted that Texaco's flights were not subject to the Section 4261 transportation tax and that Texaco was either the owner of the aircraft on which it flew or the lessee of the aircraft from the aircraft's owners through the interchange program. EJA claimed that its only role with respect to each of the Texaco flights was that of an aircraft manager.

The fundamental issue in this case was whether the flights involved the use of an aircraft in the transportation business.

The appellate court looked to the I.R.C. § 4041(c) language, which provided that commercial aviation is defined as "any use of an aircraft . . . in a business of transporting persons or property for compensation or hire by air." The appellate court further looked to the dictionary definition of the term "use" as "the act or practice of using something." Webster's 3rd New International Dictionary 2523 (1986).

The Court disagreed with EJA's claim that EJA was simply an aircraft manager. The Court noted that the NetJets program served parties who were interested in acquiring flight time, not an ownership or leasehold interest in an airplane. A participant could become a NetJets participant by acquiring as little as a 1/8 interest in an aircraft and a participant might never even fly aboard the airplane in which it had purchased an interest. On the other hand, EJA was required to handle virtually all other aspects of the flights, at its own cost.

Even though Texaco was a 50% owner of a particular aircraft, the Court found that Texaco's ownership interest was highly fettered. Texaco was required to enter into the Management Agreement, the Owners Agreement, and the Interchange Agreement. Texaco could not sell or transfer the interest without the prior written consent of EJA. Any buyer had to assume the obligations under the other contracts before a transfer could take place. Participants were prohibited from using the aircraft out of a certain specified geographic area without EJA's consent.

The Court held that the substance of the transaction rather than the form is controlling. While Texaco held legal title to its 50% ownership interest, the surrounding agreements placed extensive limitations on the use of that interest.

Thus, the Court of Federal Claims' decision was affirmed.

The AHC dismissed the significance of this federal case by stating that Missouri did not have a statute similar to I.R.C. § 4041(c), defining a transportation service as being "in a business of transporting persons or property for compensation or hire by air."

Missouri statutes do not provide that transportation services are subject to sales or use tax. Accordingly, notwithstanding the fact that the Missouri statutes fail to define a transportation service, the Department still cannot tax such a service.

The point that Fall Creek is attempting to make in citing these rulings/cases is that there is very little authority out there on this issue. Obviously, a New York Advisory Opinion, a Texas Comptroller's position statement, and a federal claims court's ruling are not binding on the Missouri Administrative Hearing Commission. The point is these are the only rulings that we know of that address this issue, and common sense tells us that we should look to the analysis set forth in these rulings/cases.

The Purchase Agreement in our case specifically provides that Fall Creek is purchasing an undivided interest in an aircraft. Likewise, a Bill of Sale was executed by Raytheon purportedly transferring an undivided interest in the aircraft to Fall Creek for purposes of registration with the Federal Aviation Administration. Other than that, all evidence supports the conclusion that the substance of this transaction was that Fall

Creek entered into a contractual relationship with Raytheon whereby Fall Creek was provided with an air transportation service.

Here are the critical conditions to the sale of the interests in these aircraft:

1. Raytheon absolutely would not sell an interest in a program aircraft unless the buyer agreed to participate in the entire program;

2. For all practical purposes, a participant could not borrow against its interest in an aircraft;

3. Transfers by a participant to a third party were strictly limited;

4. If a participant disagreed with its fellow owners, the participant could not request a partition;

5. Raytheon, at its sole discretion, could substitute a completely different airplane than the one listed in the participant's Bill of Sale;

6. Raytheon is solely responsible for inspections, insurance, maintenance, service, repair, etc.;

7. Raytheon takes care of all record keeping and compliance issues;

8. Raytheon trains and provides pilots for the program;

9. After a certain period of time, the participant has a mandatory obligation to sell its interest in the aircraft back to Raytheon;

10. Raytheon has a right of first refusal if a participant desires to sell its interest; and

11. Once the participant uses all of its hours, it has absolutely no right to use any of the airplanes, including the one it supposedly "owns."

The "true object" line of cases generally determines whether tangible property is the object of the sale by viewing the utility of the tangible property in light of the transaction. If the tangible property is not the end product or is of no continuing use after being employed as part of the process for which it is created, the true object is nontaxable services. Here, the participant has no use for its undivided interest in the airplane outside of the Program. The Governing Documents clearly contemplate that the participant will never own the undivided interest, absent the Program restrictions imposed by Raytheon. Once the participant uses its Program time, the interest in the aircraft invariably goes back to Raytheon.

This Court should find that the substance of what Fall Creek acquired was a transportation service. Not only does the Department lack statutory authority to tax an air transportation service, the Use Tax imposed on such a service would be an impermissible violation of 49 U.S.C. § 40116 (a copy of which is set out in the Appendix of this Brief at Page A-29).

49 U.S.C. § 40116 provides that a state may not levy or collect a "tax, fee, head charge or other charge" on (1) an individual traveling in air commerce; (2) transportation of an individual traveling in air commerce; (3) the sale of air transportation; or (4) the gross receipts from that air commerce or transportation.

II. THE ADMINISTRATIVE HEARING COMMISSION ERRED IN CONCLUDING THAT FALL CREEK IS RESPONSIBLE FOR PAYMENT OF USE TAX ON ITS OWNERSHIP INTEREST IN A FRACTIONAL AIRCRAFT OWNERSHIP PROGRAM, BECAUSE THE IMPOSITION OF THE USE TAX ON SUCH PROGRAM IS AN IMPERMISSIBLE BURDEN ON INTERSTATE COMMERCE IN VIOLATION OF THE COMMERCE CLAUSE OF THE UNITED STATES CONSTITUTION AND § 144.030, RSMo. 2000, IN THAT THE NUMBER OF FLIGHTS TAKEN INTO MISSOURI BY 713TA AND 798TA FOR THE TAXPAYER'S BUSINESS DO NOT CREATE A SUBSTANTIAL NEXUS UNDER THE TESTS SET FORTH BY THIS COURT IN *DIRECTOR OF REVENUE V. SUPERIOR AIRCRAFT LEASING CO.*

A. Standard of Review.

On this point, the issue is whether the AHC erred in ruling that, under the facts, the imposition of the use tax is constitutionally permissible under the tests set forth in *Superior Aircraft*. The facts are not in dispute. Accordingly, this Court's review of this issue is *de novo*.

B. Legal Authority.

In *Director of Revenue v. Superior Aircraft Leasing Co.*, 734 S.W.2d 504 (Mo.banc 1987), the Missouri Supreme Court rejected the "taxable moment" analysis set

forth in *King v. L & L Marine Service*, 647 S.W.2d 524 (Mo.banc 1983). *Superior Aircraft* involved the application of the Use Tax to an airplane that was hangared in Ohio but that logged approximately eighteen percent (18%) of its total flight hours in flights to Missouri solely for the business purposes of the taxpayer.

The Court noted that it had previously determined the applicability of the Use Tax by following the "taxable moment" analysis. Generally, the "taxable moment" analysis involved the theory that a tax does not burden interstate commerce when a period of time is found during which the property has reached the end of its interstate movement and has not yet begun to be consumed in interstate operations. If such a "taxable moment" could not be verified, the tax would impose an impermissible burden on interstate commerce.

In *Superior Aircraft*, however, the Missouri Supreme Court concluded that the "taxable moment" analysis was no longer the proper method for determining the validity of the Use Tax. Instead, the Supreme Court adopted the tests first set forth in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), as follows:

> No state tax may be sustained unless the tax: (1) has a substantial nexus with the state; (2) is fairly apportioned; (3) does not discriminate against interstate commerce; and (4) is fairly related to the services provided by the state.

In *Superior Aircraft*, the court noted that for a period beginning on April 2, 1980 and ending in September of 1981, 17.7% of the total flight hours for the aircraft in question were logged on flights to Missouri solely for Superior Aircraft's business. The

time the aircraft spent in Missouri with respect to each trip ranged from several days to approximately one week. The Court determined that these contacts were sufficient to create a "substantial nexus" in accordance with the *Complete Auto Transit* test.

Because Superior Aircraft was a Missouri corporation and maintained a business office in Missouri, the board meetings held as a result of the flights were conducted in accordance with Missouri law and the company could have used Missouri state courts to enforce resolutions arising from such board meetings. Therefore, the Court held that the tax was "fairly related" to the services provided by the state.

The Court further held that the tax imposed was "fairly apportioned" because Superior Aircraft had not paid sales or use tax in any other state and, even if it had done so, the State of Missouri had a procedure in place whereby Superior Aircraft would be given a credit for taxes paid in other states.

Finally, the remaining element of the test, involving whether the tax was discriminatory, was satisfied because Missouri's use tax did not make a distinction between interstate and intrastate business.

C. Legal Analysis.

In the Decision, the AHC correctly analyzed *Superior Aircraft* but failed to correctly apply the facts of this case.

In summary, the AHC pointed to the following factors in determining that the imposition of the use tax against Fall Creek was consistent with the United States Constitution:

1. Fall Creek was a Missouri corporation with its principal place of business located in Branson, Missouri;

2. Fall Creek used the aircraft in which it owns fractional interests, as well as other aircraft in the interchange program, for flights to and from Missouri;

3. Although Fall Creek logged less than 18% of the total flight hours of the aircraft involved, this was because Fall Creek owned only a fractional interest in the aircraft in question; and

4. This Court has never determined that 18% of total flight hours was the minimum threshold for purposes of determining nexus.

A more thorough review of the factors in this case and *Superior Aircraft* is necessary.

In *Superior Aircraft*, this Court specifically found that flights into the State of Missouri for the taxpayer's business equaling 17.7% of the total flights for a particular aircraft during the period in question create a "substantial nexus" with Missouri. While this Court did not specifically state that 17.7% was the minimum percentage of total contacts with Missouri required to create such a nexus, it is the only guidance that this Court has given with respect to these particular circumstances.

During the Audit Period, Fall Creek contacted Raytheon on sixty-seven (67) occasions in order to utilize the Program. The records reflect that Fall Creek took sixty-seven (67) flights which originated in Missouri and sixty-seven (67) flights which returned to Missouri during the Audit Period. Of those, fourteen (14) flights were intrastate flights. However, the number of times that Fall Creek utilized the Program is

irrelevant. The Department is arguing that what is subject to the Use Tax is Fall Creek's "ownership" and use of a percentage interest in a particular aircraft. For the Department to argue otherwise would be to concede that the substance of what Fall Creek acquired was a transportation service rather than an ownership interest in tangible personal property. Therefore, the constitutional analysis (and statutory analysis) should not be based upon the frequency of Fall Creek's use of the Program but on Fall Creek's use of the percentage interest of the particular aircraft in question.

Fall Creek "owned" a 6.25% interest in 713TA. During the Audit Period, 713TA made eight hundred forty (840) flights. These flights were to and from points all across the country. Even Raytheon did not know exactly where 713TA would be on a day-to-day basis. (Tr. 32). Of the eight hundred forty (840) flights, 713TA made twenty-six (26) flights with a landing or departure at a location in the State of Missouri. Therefore, of all the flights that the 713TA made during the Audit Period, only three percent (3%) of the flights had contact with the State of Missouri.

Keep in mind that just because three percent (3%) of the 713TA's flights had contact with Missouri does not mean that Fall Creek actually used the 713TA on those flights. In fact, of 713TA's twenty-six (26) flights that had contact with Missouri, Fall Creek only used the 713TA eight (8) times (and this would simply be by mere chance or coincidence). Accordingly, of the eight hundred forty (840) flights that the 713TA took during the Audit Period, only nine-tenths of one percent (.9%) of those flights involved Fall Creek's use of 713TA on a flight which had contact with the State of Missouri.

The numbers on the 798TA show an even weaker connection with the State of Missouri.

Fall Creek "owned" a 12.5% interest in the 798TA during the Audit Period. During that time, 798TA was involved in eight hundred ninety-seven (897) flights, again all over the country. Of these flights, only sixteen (16) originated in or departed from the State of Missouri. In other words, only 1.8% of all 798TA's flights during the Audit Period had contact with the State of Missouri. Of the sixteen (16) flights that had contact with the State of Missouri, Fall Creek was on three (3) of those flights. In other words, out of all 798TA's flights, only three (3) times did Fall Creek use the 798TA in Missouri (or anywhere else, for that matter). This means that Fall Creek flew on the 798TA into or out of Missouri a total of three-tenths of one percent (.3%) of 798TA's total flights during the Audit Period.

In *Superior Aircraft*, it was the percentage of flights taken into Missouri *for the taxpayer's business* that created the substantial nexus. The same test should apply in this case. With respect to 713TA, only nine-tenths of one percent (.9%) of 713TA's total flights were taken into Missouri solely for Fall Creek's business. With respect to 798TA, only three-tenths of one percent (.3%) of 798TA's total flights were taken into Missouri solely for Fall Creek's business.

Fall Creek did not utilize 713TA or 798TA for any instrastate flights. (Joint Exhibit D).

713TA and 798TA's minimal contacts with the State of Missouri do not constitute a "substantial nexus" under *Complete Auto Transit* and *Superior Aircraft*.

The second requirement under *Superior Aircraft* and *Complete Auto Transit* is that the tax be "fairly apportioned." Here, Fall Creek used the 713TA .9% and the 798TA .3% of the respective airplane's total flights during the Audit Period. The Department is seeking to impose the Use Tax as if 713TA and 798TA were used exclusively in Missouri. Simply because there is a procedure in place whereby Fall Creek *could* receive a credit for sales or use tax paid to another state does not relieve the Department's obligation to fairly apportion the tax in accordance with well established constitutional principles. The Department has failed in this regard.

Fall Creek concedes that the third requirement of the test is met due to the fact that there is a procedure in place whereby Fall Creek could receive credit for taxes paid to another state.

However, with respect to the fourth element of the test, the Department cannot justify that a Forty-nine Thousand Nine Hundred Twenty-eight and 79/100 Dollar ($49,928.79) tax on Fall Creek's utilization of 713TA and 798TA on such a limited basis is "fairly related" to any service provided by the State of Missouri. To the contrary, such an exorbitant tax under these circumstances seems completely unfair.

In summary, both the United States Supreme Court and the Missouri Supreme Court have set forth clear guidelines on whether the State of Missouri may tax an item which has limited contact with the State of Missouri. The contacts that 713TA and 798TA had with Missouri are limited in number and fleeting in substance. As such, the imposition of the Use Tax under these circumstances is unconstitutional.

III. THE ADMINISTRATIVE HEARING COMMISSION ERRED IN CONCLUDING THAT FALL CREEK IS RESPONSIBLE FOR PAYMENT OF USE TAX ON ITS OWNERSHIP INTEREST IN A FRACTIONAL AIRCRAFT OWNERSHIP PROGRAM, BECAUSE FALL CREEK HAS NOT EXERCISED SUFFICIENT DOMINION OR CONTROL OVER THE INTERESTS IN EACH AIRCRAFT TO CONSTITUTE "STORAGE" OR "USE" OF AN AIRCRAFT IN THE STATE OF MISSOURI UNDER §§ 144.610 AND 144.605(13), RSMo. 2000, IN THAT RAYTHEON MAINTAINED CONTROL OF THE AIRCRAFT AND FALL CREEK MERELY CONTACTED RAYTHEON TO REQUEST TRANSPORTATION TO A PARTICULAR LOCATION.

A. Standard of Review.

On this point, the issue is whether the AHC erred in ruling that, under the facts, the property in question was stored, used or consumed within the State of Missouri under § 144.610. The facts are not in dispute. Accordingly, this Court's review of this issue is *de novo*.

B. Legal Authority.

RSMo. § 144.610 specifies that a tax is imposed for the privilege of *storing, using or consuming* within the state articles of tangible personal property. Assuming *arguendo* that the interests in the Program acquired by Fall Creek constitute tangible personal

property, Fall Creek's utilization of the Program does not rise to the level of storage, use or consumption as contemplated in § 144.610.

The term "storage" is defined as the keeping or retention in Missouri of tangible personal property. There has been no suggestion by the Department that Fall Creek kept or retained this aircraft, or any other aircraft, in Missouri.

The term "use" is defined as the exercise of any right or power over tangible personal property incident to the ownership or control of that property. RSMo. 2000, § 144.605(13). The term "consumption" is not defined in the use tax law.

C. <u>Legal Analysis</u>.

The AHC found that because Fall Creek was in operational control of the aircraft, while in the air, Fall Creek actions constituted "use" under the statute. This was because, according to the AHC, the statute provides that "use" means "***any*** right or power over tangible personal property incident to the ownership or control of that property."

A more thorough analysis of both the Program and the aircraft in question is necessary to determine whether Fall Creek stored, used or consumed any interest within the State of Missouri.

Under the Governing Documents, Fall Creek was deemed to be in "operational control" of the aircraft only while the airplane was in the air. (Tr. 29). Other than that particular contractual provision, the Governing Documents provide that Raytheon was responsible for all other matters pertaining to the airplanes in question. Raytheon was solely responsible for the aircraft being inspected, maintained, serviced, repaired, overhauled, and tested in accordance with approved Federal Aviation Administration

standards and guidelines. Raytheon maintained all records, logs, and other materials required by the FAA to be maintained with respect to the aircraft. Raytheon retained the right to use the aircraft for training and sales promotions during periods it was not being used by the "owners." Raytheon provided and paid for all of the pilots, weather services, communication services, and all other services necessary to get the airplanes from point A to point B.

As a contractual and practical matter, Fall Creek maintained no dominion and control over 713TA or 798TA. Combined, 713TA and 798TA flew one thousand seven hundred thirty-seven (1,737) flights during the Audit Period. Of those one thousand seven hundred thirty-seven (1,737) flights, Fall Creek flew on either 713TA or 798TA a total of eleven (11) times. The only affirmative action taken by Fall Creek to cause those planes to come into the state was to make a phone call to Raytheon and ask Raytheon to have some airplane (although they did not specifically request either the 713TA or 798TA) pick up Fall Creek's employees at a particular location and transport them to another location.

The imposition of a tax on the use of property in Missouri is controlled, not only by statute, but by well established constitutional principles set forth by this Court. Accordingly, the application of § 144.610 should require an exercise of control by Fall Creek far greater than the control exercised by Fall Creek in this case.

IV. THE ADMINISTRATIVE HEARING COMMISSION ERRED IN CONCLUDING THAT FALL CREEK IS RESPONSIBLE FOR PAYMENT OF USE TAX ON ITS OWNERSHIP INTEREST IN A FRACTIONAL AIRCRAFT OWNERSHIP PROGRAM, BECAUSE THE INTEREST IN THE AIRCRAFT PURCHASED BY FALL CREEK DID NOT "FINALLY COME TO REST" WITHIN THE STATE OF MISSOURI AS REQUIRED BY § 144.610, RSMo. 2000, IN THAT THE UNDISPUTED EVIDENCE SUBMITTED AT THE HEARING BEFORE THE ADMINISTRATIVE HEARING COMMISSION INDICATES THAT 713TA AND 798TA NEVER CAME TO REST IN THE STATE OF MISSOURI.

A. Standard of Review.

On this point, the issue is whether the AHC erred in ruling that, under the facts, the interest in the program was subject to the use tax because the interest purchased by Fall Creek did not "finally come to rest" within the State of Missouri as required by § 144.610, RSMo. 2000. The facts are not in dispute. Accordingly, this Court's review of this issue is *de novo*.

B. Legal Authority.

RSMo. § 144.610 provides that the Use Tax "does not apply with respect to the storage, use or consumption of any article of tangible personal property purchased, produced or manufactured outside this state until the transportation of the article has

finally come to rest within this state or until the article has become co-mingled with the general mass of property of this state."

C. Legal Analysis.

Assuming *arguendo* that the interests in the Program acquired by Fall Creek constitute tangible personal property, any such interest did not "finally come to rest within this state" or "become co-mingled with the general mass of property of this state" as required by RSMo. § 144.610.

Fall Creek recognizes that the "taxable moment" concept was rejected by the Missouri Supreme Court in *Superior Aircraft*.

However, it should be noted that whether the imposition of the Use Tax violates the Commerce Clause of the United States Constitution is secondary to whether the Department may impose a use tax pursuant to state statute, in this case, RSMo. § 144.610. The fact that the United States Supreme Court has abandoned the taxable moment doctrine under the commerce clause should have no effect on the applicability of § 144.610. Pursuant to § 144.610, the object upon which the Department is seeking to impose the Use Tax must still "finally come to rest" in Missouri.

The AHC commission incorrectly analyzes the statutory language of § 144.610 in the context of *Superior Aircraft*. Simply put, *Superior Aircraft* did not address this issue. This is a statutory requirement separate and apart from the *Superior Aircraft* case.

This was the exact issue in *Nubo, Ltd. v. Director of Revenue*, No. RS-84-1778 (Mo. Administrative Hearing Commission, December 30, 1987). *Nubo* involved the purchase of an airplane by a Missouri corporation having its principal place of business in

Missouri. The airplane was used as a commercial aircraft for hire and was hangared and serviced between flights in Nebraska. At the hearing on the case, the parties apparently stipulated to facts concerning the circumstances of the aircraft's use in Missouri. The Commission in *Nubo* noted that the aircraft had landed in Kansas City on several occasions for the purpose of loading and unloading passengers. The record, however, disclosed no intrastate flights in Missouri and no incidents of hangaring or maintenance in Missouri.

The Commission noted that, notwithstanding whether the imposition of the Use Tax could be sustained with respect to the Commerce Clause analysis, the Commission must first determine whether the Use Tax statute itself authorized a levy of Use Tax under these circumstances. Based upon the stipulated facts, the Commission could not find that the taxpayer's aircraft had ever come finally to rest within the state or had become commingled with the state's general mass of property. Therefore, no statutory use tax liability had ever attached and a Commerce Clause analysis was unnecessary.

Pursuant to the undisputed testimony of Bill Wallisch, Vice President of Finance for Raytheon, the airplanes in the Program (including the 713TA and 798TA) are transient. The airplanes in the Program are never hangared (except in poor weather to protect the airplanes). The airplanes spend the night at whatever location is most convenient pursuant to Raytheon's optimization program. Raytheon does not even know until twenty-four (24) hours ahead of time where a particular airplane will be located. The nature of the Program is such that all of the airplanes in the Program never come to rest in any location.

Of the 840 flights 713TA took during the Audit Period, only 26 had a landing or departure in Missouri. Of the 897 flights 798TA took during the Audit Period, only 16 had a landing or departure in Missouri.

The Department put on no evidence to suggest that 713TA or 798TA ever came to rest in Missouri. All evidence presented by Fall Creek was that the airplanes never came to rest anywhere.

A requirement of § 144.610 is that the object of the use tax must "finally come to rest" within the State of Missouri. In order to impose the use tax, this Court must find that both 713TA and 798TA had "finally come to rest" within the State of Missouri. The facts in evidence do not support such a conclusion. The AHC failed to follow its own precedent on this issue.

CONCLUSION

For the foregoing reasons, Fall Creek asks that the Court reverse the AHC's decision and find that the interests purchased by Fall Creek in Raytheon's Fractional Aircraft Ownership Program are not subject to the Use Tax.

Respectfully submitted,

HUSCH & EPPENBERGER, LLC

By: _____
KENNETH N. HALL, #52474

1949 E. Sunshine St., Suite 2-300
Springfield, MO 65804
Office: (417) 862-6726
Fax No: (417) 862-6948

Attorneys for Appellant

IN THE SUPREME COURT OF MISSOURI

FALL CREEK CONSTRUCTION COMPANY, INC.,	)	
	)	
Appellant,	)	
v.	)	Case No. SC84917
	)	
DIRECTOR OF REVENUE, STATE OF MISSOURI,	)	
	)	
Respondent.	)	

CERTIFICATE OF COMPLIANCE WITH RULE 84.06
AND CERTIFICATE OF SERVICE

STATE OF MISSOURI)
) ss.
COUNTY OF GREENE)

Pursuant to Rule 84.06(c), counsel for Appellant certifies that this brief complies with the limitations contained in Rule 84.06(b). There are 11,021 words in this brief. Counsel for Appellant relied on the word count of his word processing system in making this certification.

Pursuant to Rule 84.06(g), counsel for Appellant certifies that the disk filed herewith has been scanned for viruses and is virus-free.

Further, counsel for Appellant states that Appellant's Brief in the within cause was by him caused to be served, either by hand delivery or by ordinary mail, postage prepaid, in the following stated number of copies, addressed to the following named persons at the addresses shown, all on this 10th day of February, 2003:

10 copies + disk copy: Mr. Thomas F. Simon
Clerk of the Supreme Court of Missouri
P.O. Box 150
Jefferson City, MO 65102

1 copy + disk copy: James Layton
Missouri Attorney General's Office
P.O. Box 899
Jefferson City, MO 65102

HUSCH & EPPENBERGER, LLC

By:_____
KENNETH N. HALL, #52474

1949 E. Sunshine St., Suite 2-300
Springfield, MO 65804
Office: (417) 862-6726
Fax No: (417) 862-6948

Attorneys for Appellant

Subscribed and sworn to before me this _____ day of February, 2003.

_____
Notary Public

My commission expires: